Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Developing a Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
	)	

REPLY COMMENTS OF PAC-WEST TELECOMM, INC., US LEC CORP., RCN TELECOM SERVICES, INC., CAVALIER TELEPHONE, LLC, BROADVIEW NETWORKS, INC., BRIDGECOM INTERNATIONAL, INC., AND TELCOVE OPERATIONS, INC.

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Dated: July 20, 2005

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SUMMARY

The initial comments filed in this proceeding make clear that any Order resulting from the FNPRM will have extremely far-reaching effects on the telecommunications industry. Because cost-based intercarrier compensation is such a vital component of an efficient telecommunications market, the Commission must proceed cautiously in order to achieve important policy goals while causing only as much disruption as is reasonably necessary. Radical approaches to intercarrier compensation reform, such as the proposal offered by the Intercarrier Compensation Forum (ICF), have extremely limited support and should be rejected by the Commission not only as demanding too much change too soon for all industry participants to implement, but also as being inconsistent with the law. A more reasonable and legally sustainable approach is evident from numerous commenters: the Commission must first and foremost unify all of the disparate intercarrier compensation mechanisms into a single cost-based compensation regime that makes no distinction between type of carrier or jurisdiction of the call or identity of the calling party or called party.

Further, in connection with the establishment of a single compensation regime that covers all types of traffic and all carriers, the Commission must respect the jurisdiction of state commissions over the regulation of intrastate services, particularly intrastate access charges. Preemption of the States' authority would be unwise, not justified, and ultimately counterproductive; the Commission can assume that any Order that comes out of this proceeding will face legal challenges and the Commission is more likely to prevail in those legal challenges if the States are allied with the Commission.

There is strong industry opposition to mandatory bill-and-keep arrangements. BellSouth and Verizon have now taken the position that mandatory bill-and-keep arrangements would be

inefficient. Other parties share the view that mandatory bill-and-keep is not permissible under the Telecom Act. The Commission should adopt cost-based intercarrier compensation mechanisms rather than impose inefficient bill-and-keep arrangements. BellSouth, Verizon, most CLECs and all commenting state commissions agree that cost-based intercarrier compensation is the best alternative.

The Commission should not revise the network interconnection requirements that have been reached through substantial litigation to date. The Commission should retain the single POI per LATA requirement and permit carriers interconnecting with the ILEC to determine the point of network interconnection. The legal sufficiency of single POI per LATA has been affirmed by the courts. The Commission should, however, take the opportunity to affirm that tandem transit service is a requirement imposed on ILECs by section 251(c)(2) of the Telecom Act, and tandem transit services must be provided at TELRIC.

Several Commenters provided intercarrier compensation proposals in their comments for the first time, or have offered variations on existing reform proposals. None of the new proposals are acceptable in their current form, and all would have to be revised to be seriously considered.

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REPLY COMMENTS OF
PAC-WEST TELECOMM, INC., US LEC CORP.,
RCN TELECOM SERVICES, INC., CAVALIER TELEPHONE, LLC,
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Pac-West Telecomm, Inc., US LEC Corp., RCN Telecom Services, Inc., Cavalier Telephone, LLC, Broadview Networks, Inc., Bridgecom International, Inc., and TelCove Operations, Inc. (collectively "Commenting CLECs"), submit these reply comments in response to the initial comments filed regarding the Further Notice of Proposed Rulemaking on intercarrier compensation reform of March 3, 2005.[1]

I. INTRODUCTION

The initial comments filed in this proceeding make clear that any Order resulting from the FNPRM will have extremely far-reaching effects on the telecommunications industry. Because cost-based intercarrier compensation is such a vital component of an efficient telecommunications market, the Commission must proceed cautiously in order to achieve important policy goals while causing only as much disruption as is reasonably necessary. Radical approaches to intercarrier compensation reform, such as the proposal offered by the

Intercarrier Compensation Forum (ICF), have extremely limited support and should be rejected by the Commission not only as demanding too much change too soon for all industry participants to implement, but also as being inconsistent with the law. A more reasonable and legally sustainable approach is evident from numerous commenters: the Commission must first and foremost unify all of the disparate intercarrier compensation mechanisms into a single cost-based compensation regime that makes no distinction between type of carrier or jurisdiction of the call or identity of the calling party or called party. As BellSouth says, these multiple and disparate rates for similar functions are "the most pernicious deficiency" in the current system. BellSouth Comments at 32. All other types of reform to universal service funding, interconnection obligations, and even end user rates must be subordinate to the unification of the compensation regimes and must be undertaken only upon a showing that such reform is necessary. Further, in connection with the establishment of a single compensation regime that covers all types of traffic and all carriers, the Commission must respect the jurisdiction of state commissions over the regulation of intrastate services, particularly intrastate access charges. Preemption of the States' authority would be unwise, not justified, and ultimately counterproductive; the Commission can assume that any Order that comes out of this proceeding will face legal challenges and the Commission is more likely to prevail in those legal challenges if the States are allied with the Commission.

[1] *Developing a Unified Intercarrier Compensation Regime*, Further Notice of Proposed Rulemaking, CC Docket No. 01-92, FCC 05-33, (rel. Mar. 3, 2005) ("*FNPRM*").

II. THE INITIAL COMMENTS HIGHLIGHT THE KEY AREAS OF DISPUTE

The initial comments have made clear what the key areas of dispute are in this proceeding and how the Commission should proceed to maximize the likelihood of advancing key policy goals while minimizing the risk of a subsequent successful legal challenge.

A. The Commission Need Not Decide Whether It Has the Statutory Authority to Regulate Intrastate Access Services

It should come as no surprise that the States have opposed any proposals that require the Commission to preempt State commission authority in order to establish a unified intercarrier compensation regime. NARUC takes aim at the plan proposed by ICF that requires such preemption and labels it as "a guarantee to the FCC of protracted and likely unsuccessful litigation." NARUC Comments at 3. Other states—including Texas, Maine, Vermont, Nebraska, New Jersey, Missouri, Ohio, Indiana and Iowa—express their views that the Commission should not adopt any plan that usurps their regulatory authority. No state concedes that the Commission has the authority to preempt the states; these arguments come only from Qwest, BellSouth, USTA, and the ICF. Verizon appears to wish that the Commission could preempt the States, but realizing it cannot, asks the Commission to seek the necessary statutory authority from Congress. Verizon Comments at 38.

The BOC arguments in favor of preemption are not persuasive. Qwest asserts that intrastate access charge requirements remain in place only temporarily until the Commission replaces them as described in section 251(g). Qwest Comments at 5, 23. BellSouth and ICF add a bit more meat to this argument by explaining that intrastate access charges are the result solely of the AT&T and GTE consent decrees of 1982, and since section 251(g) refers to these consent decrees, intrastate access charges necessarily fall within the scope of section 251(g). BellSouth Comments at 43-44; ICF Comments at 43. Yet these arguments do not adequately address the point that the Commission has already acknowledged, namely that section 251(g) does not apply to intrastate services. PUCO Comments at 9.

Alternatively, BellSouth asserts that the Commission may preempt the states if state commission participation in the regulatory scheme presents obstacles to achieving legitimate federal goals. BellSouth Comments at 44. It follows, according to BellSouth, that current disparate intrastate access rates impede a federal goal of uniformity, so federal preemption is justified. *Id.* at 45. The Missouri PSC provides a reasonable response to this point: the criteria for preemption cannot be satisfied as long as states can regulate intrastate services in a manner consistent with a federal unified intercarrier compensation scheme because state participation must first frustrate federal policy goals before preemption is justified. Missouri PSC Comments at 15. The Commission simply has no evidence yet that states will defy or subvert some federal policy.

It is clear that there are plausible arguments that will be made on both sides regarding the Commission's ability to preempt the states in order to establish a single, federally supervised intercarrier compensation regime. What is also clear is that such an approach is not necessary. All of the States commenting in this proceeding have indicated a willingness to participate in intercarrier compensation reform, and the NARUC Intercarrier Compensation Task Force has performed admirably to try to reach an industry consensus. The States seem amenable to a unified collaborative approach in which the FCC provides guidelines for an intercarrier compensation regime that the States would implement. The Commission should take this approach that reduces the potential conflicts with the States, retains their expertise in oversight of intercarrier agreements, and grants them some flexibility in tailoring intercarrier compensation reforms to fit particular local needs. As the comments make clear, some of the most difficult issues involve rural carriers. State commissions are clearly in a better position to evaluate and address those concerns than the FCC.

There is little to be gained by preempting the states on the issue of intercarrier compensation and much to be lost. The Commission is not equipped to handle the inevitable disputes that will arise over non-payment that State commissions currently handle. If only enforcement authority is delegated to the States, how willing does the Commission expect States to be to handle limited delegated authority to resolve disputes, without the authority to establish any of the rules or requirements underlying intercarrier compensation disputes?[2] The answer is that encroaching on state commission jurisdiction is likely to result in virtually all intercarrier compensation enforcement being passed off to the Commission. One can expect the carriers with the market power and the incentive to withhold payment of intercarrier compensation to take advantage of the vastly increased enforcement workload at the Commission.

B. The Initial Comments Illustrate Strong Industry Opposition to Mandatory Bill-and-Keep

Any intercarrier compensation reform proposal that requires carriers to adopt bill-and-keep arrangements has strong opposition within the industry. All of the State commissions oppose mandatory bill-and-keep, with NARUC going so far as to say that it will not endorse *any* proposal that mandates bill-and-keep. NARUC Comments at 3. BellSouth makes a strong case against bill-and-keep at this time, even though it advocated for bill-and-keep in the 2001 proceeding. BellSouth Comments at 9. BellSouth shares the views of other bill-and-keep opponents: it would not promote economic efficiency or preserve universal service; it would not

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[2] Of course, there is no assurance that attempting to delegate enforcement to state PUCs would not run into legal challenges by certain carriers.

be competitively neutral; bill-and-keep is premised on assumptions about the market that have no basis; it would undermine contract negotiations between carriers by eliminating intercarrier compensation; and by adopting bill-and-keep the Commission would be substituting its own judgment for market forces regarding when carriers would choose to adopt bill-and-keep arrangements. BellSouth Comments at 9-12. BellSouth also makes clear that it would consider mandatory bill-and-keep to violate the Takings Clause of the U.S. Constitution. BellSouth Comments at 12 n.20.

Verizon has also backed away from any support for bill-and-keep. To Verizon, mandatory bill-and-keep cannot produce efficient results. Verizon Comments at 2. Verizon says bill-and-keep would provide disincentives for network investment and would encourage a whole new host of arbitrage opportunities. *Id.* at 3-4, 22.

Commenting CLECs actually agree with Verizon and BellSouth in this instance. While bill-and-keep arrangements certainly have some benefits because they eliminate the need to implement billing and collection systems to collect certain kinds of compensation from other carriers, they do not eliminate the collection of all kinds of compensation from other carriers and carriers will continue to collect information on incoming and outgoing traffic in order to properly engineer facilities. The benefits of bill-and-keep are limited, and to the extent a carrier wishes to take advantage of those benefits, it may do so on a voluntary basis. For some carriers bill-and-keep may prove to be worthwhile; for all of the others, it certainly would not.

Moreover, the comments support Commenting CLECs' view that mandatory bill-and-keep is unlawful. *See* Commenting CLECs Initial Comments at 13-15. The New York Department of Public Service agrees that mandatory bill-and-keep would violate the Telecom Act. NYDPS Comments at 7. The Public Utilities Commission of Ohio also agrees with

Commenting CLECs that bill-and-keep could not satisfy the "additional cost" standard of section 252, while the cost-based compensation advocated by Commenting CLECs "always" would. PUCO Comments at 18.

At the same time, Commenting CLECs disagree with those parties that seek to limit the scope of section 251(b)(5) to only "local" or non-interexchange traffic. *See, e.g.*, Verizon Comments at 34, 40-41; Maine PUC and Vermont PSB Comments at 7; NYDPS Comments at 9-10. There is no such limitation in the statute, and the Commission itself has recognized that section 251(b)(5) applies to all telecommunications not expressly carved out by section 251(g). Commenting CLECs Initial Comments at 54-55.

From a broader perspective, however, it does not matter significantly whether section 251(b)(5) applies to interexchange traffic for the purposes of establishing a unified intercarrier compensation regime. The Commission certainly has authority to regulate all interstate communications, all CMRS communications, and all communications related to implementation of the Telecom Act through a combination of statutory authority found in sections 201, 251, and 332. As Commenting CLECs noted, section 251(b)(5) simply serves as the statutory baseline for a unified intercarrier compensation regime because it has a specific cost standard in section 252 while the other sections do not. Commenting CLECs Initial Comments at 8-9. Once the Commission established intercarrier compensation rules applicable to section 251(b)(5) using the section 252 cost standard, it could simply require intercarrier compensation rules established under section 201 and section 332 to adhere to the requirements applicable to sections 251(b)(5) and 252.

C. The Initial Comments Show Strong Support for Cost-Based Intercarrier Compensation

As stated above, the comments make clear that mandatory bill-and-keep is not lawful and therefore not an approach that the Commission should embrace. A lawful and reasonable approach to intercarrier compensation reform is to continue a calling-party's-network-pays regime at rates that apply to all traffic. A significant number of commenters agree with Commenting CLECs and endorse cost-based compensation under a forward-looking economic cost standard. *See, e.g.,* PUCO Comments at 17-20; Missouri PSC Comments at 3, 9; Ad Hoc Telecommunications Users Committee Comments at 4; XO Communications Comments at 8; New Jersey BPU Comments at 3; Time Warner Telecom, Conversent Communications, Inc., CBeyond Communications LLC, and Lightship Telecom Comments at 6-15. As Ionary Consulting states, "The Cost-Based Intercarrier Compensation Coalition proposal is by far the best of the seven [proposals] at meeting the principles" of intercarrier compensation reform. Ionary Consulting Comments at 16. Ionary Consulting adds, "Its use of TELRIC-based rates for all intercarrier compensation holds carriers essentially harmless against changes in traffic levels imposed by other carriers, and minimizes gaming. . . The CBICC plan is fully unified and technology neutral; furthermore, it is fundamentally simple. It allows a role for states in setting the appropriate rates[.]" Ionary Consulting Comments at 17. BellSouth has even proposed an intercarrier compensation reform proposal that uses default origination and termination rates that "approach current reciprocal compensation rate levels." BellSouth Comments at 17. In other words, BellSouth endorses a termination rate using the section 252(d)(2) standard for all intercarrier compensation arrangements.

Verizon even supports cost-based compensation, but at a rate higher than TELRIC because Verizon believes TELRIC requires ILECs to charge below-cost rates. Verizon

Comments at 18. USTA agrees with Verizon that TELRIC rates would be too low. USTA Comments at 23.

Once a unified cost-based regime has been implemented, the FCC will have the opportunity to evaluate the results to determine its effectiveness and whether other subsequent changes are warranted. Moving to cost-based rates for all traffic regardless of carrier or jurisdiction or identity of the called party would resolve the most significant problem associated with the current crazy quilt of intercarrier compensation regimes.

D. ILEC Revenue Neutrality Is Neither A Requirement Nor An Appropriate Goal

A key component of the proposals offered by the ILECs is the mandated recovery of all revenues lost as a result of intercarrier compensation reform. *See, e.g.,* Qwest Comments at 12; USTA Comments at 34-35. The ICF plan is essentially zero-sum, based on current intercarrier compensation revenue levels. ICF Comments at 26-28.

Commenting CLECs see merit in the views of those commenters that assert that however the Commission feels about creating opportunities for ILECs to recover lost revenues, it should not assume that existing intercarrier compensation revenue levels are some baseline that must be offset by increased revenues from some other source. *See, e.g.,* Nextel Comments at 19-21; Cox Communications Comments at 11-13; Ad Hoc Telecommunications Committee Users Committee at 11-12. While CBICC had proposed SLC increases to offset losses in interstate access charge revenues, it is possible that ILECs would have lost that revenue as a result of competition and changes in the industry, in which case it would not be appropriate to guarantee the LEC revenue base through a dollar-for-dollar SLC replacement.

Along these lines, SBC characteristically misconstrues the Cost-Based Intercarrier Compensation Coalition's proposal as requiring carriers to face dramatic reductions in intercarrier compensation revenues with no adequate opportunity to make up for the lost compensation from other sources. SBC Comments at 16. Commenting CLECs are saying nothing of the sort. Commenting CLECs think that ILECs should have the same opportunity to recover lost access charge revenues from other sources that CLECs had when the Commission slashed reciprocal compensation revenues for traffic to ISPs or CLEC access charges in general. The Commission was not terribly concerned about guaranteeing replacement revenue for CLECs when it imposed a step-down in access rates in the *CLEC Access Charge Order*.[3] The ILECs will manage without a guarantee also.[4]

E. Network Interconnection Requirements Should Not Be Changed

Many of the commenters have assumed that intercarrier compensation reform necessarily requires reform to the network interconnection requirements that have been hammered into place over the past nine years of implementation of the Telecom Act. *See, e.g.,* ICF Comments at 20-21. The assumption is questionable, and in fact, linking intercarrier compensation reform to network interconnection reform has the potential to be extremely disruptive to the industry. Commenting CLECs actually agree with Verizon on this issue: Verizon says most of the disputed issues regarding interconnection have been resolved at the state and federal levels, and any intercarrier compensation reform should preserve established arrangements. Verizon

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[3] A*ccess Charge Reform, Reform of Access Charges Imposed by Competitive Local Exchange Carriers,* Seventh Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 96-262, 16 FCC Rcd 9923 (2001) (*CLEC Access Charge Order*).

[4] Indeed, guaranteeing SBC and Verizon any sort of revenue neutrality as a condition of intercarrier compensation reform would be virtually impossible given that each is in the process of acquiring large IXCs.

Comments at 29-30. Verizon is opposed to the adoption of two new sets of rules—one for intercarrier compensation, one for network interconnection—that have never been tested in the real world. *Id*. at 31. Commenting CLECs made the same point in their initial comments. Commenting CLECs Initial Comments at 47-49. Nextel agrees that departure from the existing requirements would be highly disruptive, without serving any of the Commission's greater policy goals. Nextel Comments at 31.

BellSouth takes a subtle approach, but in the name of proposing "a minimalist approach to network architecture," actually proposes fairly onerous interconnection obligations. BellSouth Comments at 18-19. BellSouth proposes interconnection requirements in which a CLEC or CMRS carrier must interconnect at every ILEC tandem. *Id.* at 18. This is a substantial departure from the existing requirement of a single POI per LATA, and it should be readily dismissed on the same grounds that it was dismissed in the *Virginia Arbitration Order*.[5] The Commission's interpretation of the interconnection obligations of section 251(c)(2) permit CLECs to designate a single point of interconnection on the ILEC's network, and the ILEC is required to transport traffic to and from that point of interconnection.[6]

As for the ICF "Edge" proposal, Commenting CLECs have previously demonstrated how it is discriminatory to CLECs. It bears repeating that the ICF Edge proposal would impose enormous financial burdens on CLECs while also providing potentially enormous subsidies from ILECs to their wireless subsidiaries. Commenting CLECs Initial Comments at 41 n.81. The ICF

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[5] *Petition of WorldCom, Inc. Pursuant to Section 252(e)(5) of the Communications Act for Preemption of the Jurisdiction of the Virginia State Corporation Commission Regarding Interconnection Disputes with Verizon-Virginia, Inc., and for Expedited Arbitration*, 17 FCC Rcd 27039 (rel. July 17, 2002) ("*Virginia Arbitration Order*") at ¶¶ 52-53.

[6] *Id.* The Commission should take the opportunity to make clear that transport facilities between a CLEC switch and an ILEC switch are interconnection facilities under section 251(c)(2) that must be provided at TELRIC rates. *See* Commenting CLECs Initial Comments at 20.

Edge proposal should be rejected, and if any "Edge" proposal is to be considered, it should resemble something more like the Qwest Edge proposal that makes no distinction in transport obligations between "Hierarchical" and "Non-Hierarchical" networks.

Rural LECs oppose single-POI-per-LATA because it supposedly ignores the configuration of rural LEC networks. Rural Alliance Comments at 20. The Public Utilities Commission of Ohio addresses CLEC or CMRS interconnection by proposing a requirement that carriers establish traffic exchange agreements prior to sending any traffic to rural LECs for termination. PUCO Comments at 15. Commenting CLECs are not opposed to entering into traffic exchange agreements with rural LECs, but the Commission must understand that rural LECs have been extremely reluctant to enter into such agreements. CBICC has already conceded that the transport obligation of rural LECs should not extend beyond their own service boundaries. Ex Parte Letter from Richard M. Rindler, Swidler Berlin Shereff Friedman, LLP, to Marlene H. Dortch, Federal Communications Commission, dated September 2, 2004. Direct interconnection should not be required unless traffic volumes warranted it, and the parties would be clear about their responsibilities to pay for transport for calls exchanged between CLECs and rural carriers. A Commission rule that makes this obligation clear would significantly improve the likelihood of CLECs and rural LECs coming to agreement on terms for the exchange of traffic.

Commenting CLECs maintain, however, that no revision to the existing network interconnection requirements is necessary at this time, and the single-POI-per-LATA requirement should be retained because it is the only default network architecture obligation that satisfies sections 251 and 252 of the Act. Commenting CLECs Initial Comments at 48. Rather than impose specific traffic volume thresholds at which CLECs must move traffic away from a single POI—*see, e.g.,* Comments of NuVox at 5; PUCO Comments at 14—the Commission should rely instead upon the reasonable judgment of CLECs to groom their networks and interconnection facilities as traffic volumes warrant. Commenting CLECs have all demonstrated a willingness to establish direct interconnection trunks with other LECs as circumstances and sound engineering practices demand.

F. Tandem Transit is Required by the Telecom Act

The statutory obligation of ILECs to provide tandem transit services is challenged by several commenters. Commenting CLECs demonstrated how tandem transit service is a requirement imposed on ILECs by both sections 251(a) and 251(c)(2) of the Act. Because tandem transit is required by section 251(c)(2), it must be provided by ILECs at the cost standard described in section 252(d). Commenting CLECs Initial Comments at 21-22. Several parties agree with the Commenting CLECs' view that tandem transit is required by section 251(c)(2) at cost-based rates. *See, e.g.*, Cox Communications Comments at 15-19; PUCO Comments at 28; XO Communications Comments at 25-26; Nextel Comments at 11.

Two of the Bell companies now assert that they have no obligation to provide tandem transit service under any statutory provision. *See, e.g.,* Qwest Comments at 36-37; BellSouth Comments at 33-35. SBC concedes that tandem transit is a statutory requirement, but only under section 251(a). SBC Comments at 4. Verizon remains silent on the matter in its comments, but at least one company has been told by Verizon that it is unwilling to agree to provide transiting arrangements in an interconnection agreement.

The arguments advanced by Qwest and BellSouth that tandem transit is not required by section 251(c)(2) are not persuasive. Qwest claims that section 251(c)(2) is not applicable to tandem transit service because it speaks only to the ILEC duty to provide interconnection with the ILEC's network. Qwest Comments at 37. BellSouth draws a distinction between "interconnection" under section 251(c)(2) and transport. BellSouth Comments at 34-35. BellSouth's argument assumes the conclusion that tandem transit service is only a transport service and cannot be an interconnection service. BellSouth cites no authority for this argument. In fact, both arguments are wrong. Nothing in section 251(c)(2) limits the ILEC obligation in the way suggested by Qwest and BellSouth. Section 251(c)(2) requires an ILEC to provide interconnection with its network "for the transmission and routing of telephone exchange service and exchange access." This language creates no limitation on the routing of traffic to only traffic that is originated by either the ILEC or the requesting carrier. Traffic originated by or terminated to a third-party carrier also fits within the definition as long as such traffic is either telephone exchange service or exchange access (which includes all traffic exchanged between LECs). In order for a competitive carrier to transmit and route telephone exchange service to a third-party carrier, at the request of the competitive carrier, an ILEC has an obligation under 251(c)(2) to provide tandem transit service, regardless of whether one characterizes the service provided by ILEC as "interconnection" or "transport." Simply put, section 251(c)(2) permits CLECs to plug their networks into the ILEC networks at any technically feasible point in order to get telephone exchange service or exchange access wherever it needs to go.

G. "Phantom" Traffic Appears to be Primarily a Problem Between Rural LECs and Wireless Carriers

The primary concern among rural LECs appears to be the ongoing loss of a significant and traditional form of revenue: interstate and intrastate access charges. As regulated rate-of-return carriers, they expect the Commission to take some regulatory action to offset their losses. A key issue to them is so-called "phantom traffic" that comes to them from ILEC tandem switches in forms that prevents them from billing another carrier intercarrier compensation. *See, e.g.*, Beehive Telephone Comments at 3-4; Ex Parte Letter from Karen Brinkmann, Latham & Watkins, to Marlene H. Dortch, Federal Communications Commission, dated July 1, 2005. The telling feature here is that a full two-thirds of this "phantom traffic" problem apparently comes from wireless carriers. *Id.* at Slide 5. Rural LECs should probably look first to the market leaders in the wireless industry—Verizon Wireless, Cingular Wireless, Nextel and Sprint—to solve the problem of "phantom traffic." Whatever technological fixes wireless companies deploy likely could be duplicated throughout the rest of the industry. To the extent the "phantom traffic" label is intended to suggest problems with other forms of traffic, such as Foreign Exchange or Virtual NXX, that is a misnomer and will be resolved by the adoption of a unified rate for terminating all traffic.

H. The Commission Should Resolve the Remand of the *ISP Remand Order*

The initial comments also reveal the ongoing dispute over intercarrier compensation for ISP-bound traffic. Qwest and Verizon, predictably, call for an immediate ruling that no compensation whatsoever is owed for ISP-bound traffic. Qwest Comments at 8, 56; Verizon Comments at 21 n.20. SBC breaks ranks with the other BOCs and now argues that ISP-bound traffic is subject to section 251(b)(5) after all. SBC Comments at 23-24. BellSouth concedes that ISP-bound traffic is "local traffic." BellSouth Comments at 13.

Like Commenting CLECs, XO Communications urges resolution of this matter by issuing an Order immediately that would resolve the remand of the *ISP Remand Order* from the D.C. Circuit, which has now been pending before the Commission for more than three years. XO Comments at 10. The Commission should rule that ISP-bound traffic is subject to section

251(b)(5) of the Act. This ruling would be consistent not only with Commenting CLECs, MCI, AT&T, XO and others, but also with SBC Communications.

III. RESPONSE TO NEW INDUSTRY PROPOSALS

Several Commenters provided intercarrier compensation proposals in their comments for the first time, or have offered variations on existing reform proposals. None of the new proposals are acceptable in their current form, and all would have to be revised to be seriously considered.

A. BellSouth proposal

BellSouth has offered a comprehensive reform proposal that first and foremost rejects bill-and-keep and proposes uniform default rates for all traffic. At the end of all transition periods, carriers would receive $0.0025 per minute for traffic exchanged at the ILEC tandem switch, and $0.00125 for traffic exchanged at the ILEC end office switch for originating and terminating traffic by the retail service provider. Commenting CLECs are not opposed to the uniform rate structure proposed by BellSouth, but BellSouth provides insufficient details to explain the full scope of its proposal. BellSouth's proposal retains a 3:1 ratio to identify ISP-bound traffic, but for what purpose? Surely BellSouth is not proposing the elimination of all terminating compensation for ISP-bound traffic since the FCC has already eliminated the growth caps and new market restrictions that had been put in place four years ago. Further, BellSouth argues at length how switching costs are traffic-sensitive and recovery of switch costs on a usage-sensitive basis is appropriate. BellSouth Comments at 22-26. There is no reason to think that switching costs below a particular traffic-exchange ratio are traffic sensitive but switching costs above the same ratio are not. At the end of all transition periods, BellSouth's proposal should require the same terminating compensation rate for all traffic, regardless of the identity of the called party.   BellSouth's proposal must be more clear about the positive terminating compensation rate that is owed for the termination of ISP-bound traffic during the transition period and at the end of that period.

Other aspects of the BellSouth proposal would require substantial revision. For example, as discussed above, BellSouth's proposal to require interconnection at every ILEC tandem switch would not be consistent with the requirements of the Act.   As for BellSouth's proposal to revise subscriber line charge requirements, Commenting CLECs agree that there should be two categories for SLCs: Mass Market SLCs and Enterprise SLCs.   Commenting CLECs assert, however, that an ILEC should be required to recover lost access charge revenues first from enterprise customers and then from mass market customers lest the ILEC exploit its lack of competition in the mass market to subsidize its service in the more competitive market of service to enterprise customers.

B. Frontier proposal

Frontier Communications also makes an intercarrier compensation proposal, but it has little merit. In short, the Frontier proposal assumes competition in markets that does not exist so it would easily result in situations in which ILECs would be able to exploit market power.   The Frontier proposal resembles in many respects the poorly received "COBAK" proposal from 2001, with the difference of requiring capacity-based port charges at end offices rather than bill-and-keep at the end office. Commenting CLECs are not necessarily opposed to capacity-based charges in lieu of per-minute charges, but as explained in their initial Comments, the Commission should realize that capacity-based port charges have significant implementation problems and require further study. Commenting CLECs Initial Comments at 15-16.   The Frontier proposal, however, deregulates all interoffice transport. Frontier Comments at 8-9. It also imagines the creation of a market of traffic aggregators that combine deregulated transport offerings with capacity-based port access to carriers that do not provide their own transport or do not interconnect directly at LEC end offices. All of these proposals will provide enormous market power to the ILECs that are already in the position to dominate a market of unregulated transport.

Compounding the problem further, the Frontier proposal requires carriers to transport traffic (using deregulated transport services) all the way to the terminating LEC's end office. So not only would CLECs have to purchase deregulated transport services from ILECs, they would be required to purchase more of it under Frontier's proposal than they currently purchase in a regulated transport market. Frontier's proposal has free-market idealism written all over it, but it would prove to have disastrous consequences to competitors in the real world and would essentially concede ILEC domination of the local exchange market.

C. NARUC Task Force Version 7

Commenting CLECs commented at length on the previous version of the intercarrier compensation reform proposal offered by the NARUC Intercarrier Compensation Task Force. Commenting CLECs Initial Comments at 31-36. Shortly before initial Comments were filed, the Task Force released its latest iteration of its proposal, Version 7. The changes in Version 7 are small, yet very significant. Commenting CLECs maintain that substantial revisions to the Task Force proposal are necessary before it would be acceptable.

The primary change in Version 7 is to the default terminating compensation rates carriers may charge. It lowers the default rate for ILEC wire centers with more than 5000 access lines (90% of the ILEC wire centers) from $.002 to $.001 per minute. The Task Force does not give any explanation for this change, so it appears to be completely arbitrary. The revision has no clear support as a cost-based rate, since the national average is closer to $.00212. Retaining a default rate of $.002 is more likely to be sustainable as a cost-based rate that would satisfy the requirements of section 252(d)(2).

Version 7 also raises the default rate for ILEC wire centers with less than 500 access lines (1% of ILEC wire centers) from $.01 to $.02. This rate would apply only to the smallest ILECs, in all likelihood. Again, the significant rate increase has no justification and appears to be simply arbitrary. While it is theoretically possible that the smallest ILECs could have forward-looking terminating switching costs 10 times higher than the largest ILECs, it is probably not likely and would most certainly demand some reasonable demonstration of cost support.

The Task Force's Version 7 also gives the impression that an originating access charge of $.002 per minute for all carriers is now acceptable. Commenting CLECs have proposed an originating switching charge for calls dialed on a 1+ or 1-800 basis, and a rate of $.002 per minute is not objectionable. An originating rate of $.002 per minute, however, makes a terminating rate of $.001 per minute using the same switch highly questionable. While originating switching may incur greater costs than terminating switching—at least in terms of call set-up—it is extremely unlikely that originating switching costs are twice as high as terminating switching costs.

Version 7 also continues to "tentatively" adopt the ICF transport and transit proposal, but says that the possibility of combining the hierarchical and non-hierarchical categories "should be explored." The proposal recognizes that the ICF proposal may not be "appropriate." This is a good step, and one advocated by Commenting CLECs in their initial Comments, but it does not go far enough to satisfy Commenting CLECs' concerns. As discussed previously, the ICF transport and transit proposal would impose enormous and discriminatory cost burdens on CLECs. It would severely constrain the development of competitive transport markets, and it would potentially provide for subsidies from ILECs to their CMRS subsidiaries. Commenting CLECs Initial Comments at 41 n.81. The NARUC Task Force proposal is not acceptable to Commenting CLECs until it abandons the ICF transport and transit proposal.

IV. CONCLUSION

Because cost-based intercarrier compensation is such a vital component of an efficient telecommunications market, the Commission must proceed cautiously in order to achieve important policy goals while causing only as much disruption as is reasonably necessary. Radical approaches to intercarrier compensation reform, such as the proposal offered by the Intercarrier Compensation Forum, have extremely limited support and should be rejected by the Commission not only as demanding too much change too soon for all industry participants to implement, but also as being inconsistent with the law. A more reasonable and legally sustainable approach is evident from numerous commenters: the Commission must first and foremost unify all of the disparate intercarrier compensation mechanisms into a single cost-based compensation regime that makes no distinction between type of carrier or jurisdiction of the call or identity of the calling party or called party.

Further, in connection with the establishment of a single compensation regime that covers all types of traffic and all carriers, the Commission must respect the jurisdiction of state commissions over the regulation of intrastate services, particularly intrastate access charges. Preemption of the States' authority would be unwise, not justified, and ultimately counterproductive; the Commission can assume that any Order that comes out of this proceeding will face legal challenges and the Commission is more likely to prevail in those legal challenges if the States are allied with the Commission.

Respectfully submitted,

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